# THERMAL CONTROL TECHNOLOGIES CORP.



# 1998 ANNUAL REPORT

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Annual General Meeting,

October 6, 1998

3:00 to 5:30 pm

Calgary Petroleum Club

319, 5 Avenue S.W.,

Calgary, Alberta, T2P 0L5

## PRESIDENT & CEO'S LETTER TO SHAREHOLDER

The year ending March 31, 1998 has marked another year of positive developments, unparalleled growth and successes. We at TCT continue to focus on the research, development and expansion of our proprietary technology, while expanding our product line in Charge Air Coolers, Radiators and Cooling System accessories.

**Thermal Control Technologies Corp.**
**Highlights for Fiscal Year 1998**

- Revenues of $7,107,284 compared to $1,941,988 an increase to 366% of 1997

- Profit (pre tax) of $0.12 per share compared to last years $0.03

- Cash flow increased from $0.05 to $0.15 per share

- OEM Supplier to Road King of Monterrey, Mexico. Additionally TCT is a supplier to Finning (Canada) of Edmonton, Alberta, and Foremost Industries of Calgary, Alberta.

- Certification of a complete cooling package by Detroit Diesel Corporation, the largest supplier of diesel engines to the metro-bus and motor coach manufacturers in North America.

- The TCT distribution network has expanded to include 35 outlets throughout Mexico for a total of 169 in North America.

**Strategy for Continued Growth and Expansion Within our Industry**

The market for Charge Air Coolers in Canada and the U.S. alone for Class 8 trucks is 400,000 per annum. Our sales have been growing at an astonishing rate, but the industry is now just starting to accept the fact that a leaking cooler is a problem. Up until the last few years it wasn't common practice for service centers to test for leaks. TCT has helped educate the Dealers in the benefits to both their clientele and bottom line. We also believe that it is very important to educate the end-user in the benefits of our technology so that they ask for TCT products.

TCT has found the marketplace for complete cooling systems to be of strategic importance. Rather than have the end user go to our competitors for parts of the cooling system we don't supply, the plan is to eventually supply all of the components.

We are also seeking to reduce fixed costs through expansion of our business plan and the development of TCT's Prescott facility. Being able to design, test, manufacture, and assemble the majority of our products in-house will not only reduce TCT's costs, but also our dependency on outside suppliers.

TCT and I thank our shareholders for their continued support during the past year and look forward to sharing more of our successes in the years to come.

Sincerely,

Blaine Maller

*Blaine Maller*
*President & CEO*

*Board Of Directors and Senior Officers*
*Standing, left to right: Everett Koeller, Vern Maller, Bruce Harradence, Blair Hooper*

*Sitting: Kim Johnson, Blaine Maller*

# CORPORATE PROFILE

Thermal Control Technologies Corp. is a manufacturer of advanced heat exchange equipment for sale and distribution into the automotive, heavy duty truck and industrial equipment, agricultural and marine aftermarkets. TCT's flagship proprietary technology is patent pending and allows the cooling core to float which solves many of the problems associated with conventional radiator and cooling system design.

## HIGHLIGHTS

July 16, 1997 – Redux announces first quarter results. Revenues reported are $1,589,011 as compared to $146,243 for the same period one-year earlier.

September 17, 1997 – 797,578 warrants are exercised at a price of $1.35 for total proceeds of $1,076,730.

October 1, 1997 – The Corporation changes its name from Redux Energy Corporation to Thermal Control Technologies Corp.

October 24, 1998 – The ticker symbol changes from "RDX" to "TCT" on the Alberta Stock Exchange and from "RDXEF" to "TCTCF" on the NASD Bulletin Board.

November 18, 1998 – TCT reports Second Quarter revenue of $3,261,826 compared to $279,544 for the same period one-year prior.

December 19, 1997 – Convertible Debenture offering of $7,000,000 was fully subscribed. Proceeds of the issue are earmarked for development of a new manufacturing facility in Prescott, Arizona among other areas.

January 7, 1998 – Detroit Diesel Corporation certification is obtained with the TCT cooling system having met the requirements of DDC and their Series 50 turbo-charged diesel engine.

February 24, 1998 – Third quarter result are revenues of $5,368,888 as compared to $1,029,042 for the previous year.

March 2, 1998 – TCT announced that it had entered into an economic development agreement with the City of Prescott, Arizona. The new 30,000 square foot manufacturing facility will have three times the capacity of Lincoln.

1998 Year End Financials Revenues $7,107,284 vs. $1,941,988; Earnings Before Taxes $1,452,753 vs. $341,921; After Tax EPS $.09 vs. $.03 and Cash Flow $.15 vs. $05.

OEM Supplier to Road King of Monterrey, Mexico. As well TCT is a supplier to Finning (Canada) of Edmonton, Alberta, and Foremost Industries of Calgary, Alberta.

## LOCATIONS

Calgary, Alberta – Administration for all TCT locations and Canadian Sales are conducted from the head office in Calgary.

Edmonton, Alberta – TCT manufactures custom cooling packages and offers radiator repair at this facility. Custom packages have been manufactured for stationary diesel generators (gen-sets), buses, service rigs, and drill floor motors. Caterpillar folded core conversions are another offering out of our Edmonton location. The custom kits for Finning (Canada) are manufactured and distributed in Edmonton. Specifically designed for the electronically controlled gen-sets, the Finning (Canada) packages consist of a radiator, charge air cooler, internal surge tank, fan, shroud, and belt guard.

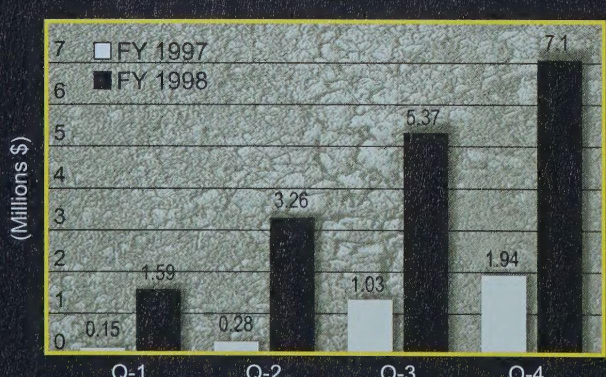
Lincoln, Nebraska – All TCT charge air coolers and test kits are manufactured in Lincoln. As well, the U.S. sales team is based out of Lincoln.

Prescott, Arizona – This new 30,000 square foot facility is under construction and TCT plans to hold the ribbon cutting ceremony during September 1998. Prescott will have the capacity to build 3,000 CACs and 200 radiators per month, which is triple the existing capacity of the Lincoln facility. Enough land has been purchased to further expand the plant to three times its original size.

## PRODUCTS

**Charge Air Coolers:**
CACs are produced for the following Class 8 trucks: Freightliner, Kenworth, Peterbilt, Navistar, International, Mack, and Volvo. Custom designed CACs are also offered for any application.

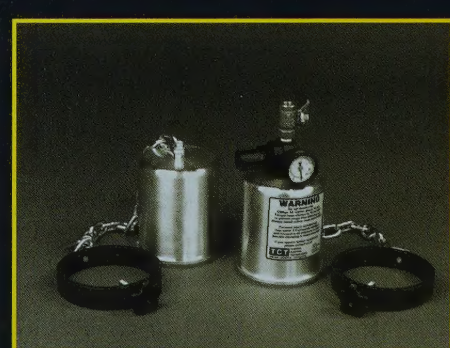
**Complete cooling packages:**
These consist of several or all of the following, radiator, CAC, fan, shroud, belt guards, and internal surge tank.




*CUMULATIVE QUARTERLY REVENUES*

**HIGH & LOW STOCK PRICES ($Can.)**

**High: $2.19**
**Low: $1.25**



*TCT Test Kit*

**Test kits:**
The TCT test kit is listed in a Detroit Diesel service bulletin and a Freightliner shop manual. Both state that Charge Air Coolers should be tested using the Thermal Control Technologies test kit and they even list our phone number to order it. It is difficult to determine if a CAC is leaking through visual inspection, because it doesn't leave physical evidence like a radiator does when leaking coolant. Service departments can generate additional sales by using the test kit. The test for leakage on a CAC is very simple. With the WK – 93(P) test kit installed the CAC is pressurized to 30 (25lbs for some manufacturers) pounds per square inch (psi), over the next 15 seconds if pressure decay is 5 psi or more then the CAC is considered defective and must be replaced. TCT CACs are factory tested to 40psi ensuring a complete seal. The reality is a 3-4 psi leak can reduce fuel economy by up to 1/2 MPG. On a vehicle which only gets 3-4 MPG, 1/2 MPG is a substantial difference.

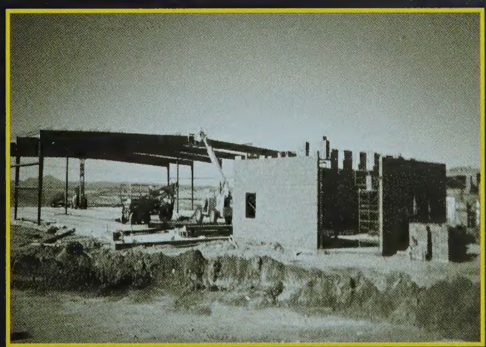
## CERTIFICATION FROM DETROIT DIESEL CORP.

Las Vegas was the location for testing of a complete cooling system consisting of a charge air cooler, radiator, fan, and shroud assembly. The complete package was installed on a metro-transit bus manufactured by the New Flyer Bus Company of Winnipeg, Manitoba. The TCT cooling system met the requirements of Detroit Diesel Corporation's Series 50 turbocharged diesel engine. Detroit Diesel is the largest supplier of engines to the current North American manufacturers of metro-transit systems and motor coaches.

## NEW MANUFACTURING FACILITY

Prescott, Arizona has been chosen by TCT as the location for the new manufacturing facility. C.J. Moss Co. was retained to survey locations around the United States and determine the most advantageous region for TCT. The State of Arizona and the City of Prescott have advantages for TCT's purposes which are far above and beyond those offered by any other region in the United States. Some of the benefits are: State tax incentives, City of Prescott incentives, financial assistance from the Arizona Department of Commerce in the form of an Industrial Development Bond financing (the bond will be offered at a lower interest rate because it is tax-exempt) and a State sponsored job training programme at Yavapai County College.





*The new 30,000 square foot manufacturing facility under construction in Prescott, Arizona will have the capacity to build 3,000 CACs and 200 radiators a month.*

## FUTURE

There are many other applications besides Class 8 trucks which use CACs including stationary generators, buses and oilfield equipment. These are very large markets for both complete cooling systems and CACs. The complete cooling packages which TCT offers have been a great success for the Company to date and sales have been increasing at a more rapid pace than what was previously expected. Consequently, we will be looking to expand these markets as well.

Our Sales team has contacted the Class 8 truck manufacturers about becoming an Original Equipment Manufacturer (OEM) Supplier. The sales cycle to become an OEM supplier is quite long and currently, TCT would only be able to supply the smaller manufacturers, but our Sales people continually follow up with Companies of all sizes. As well, TCT has applied for ISO 9000 certification since management sees this as a prerequisite for all OEM contracts in the future.

TCT's gasket technology is transportable into many other products such as, oil & transmission coolers, air conditioning condensers and of course radiators. As we continue to grow these are additional areas in which TCT will look to expand.

## MANAGEMENT DISCUSSION AND ANALYSIS

Items related to inventory and manufacturing have increased due to the growth and expansion of TCT as a company. The most notable change has been the increase in property, plant and equipment. The increase from $3,175,237 to $10,733,745 has been predominantly for the Prescott operation.

**Consolidated Statement of Earnings and Retained Earnings:**

Revenues of $545,513 were carried into the first quarter of 1998 from the fourth quarter of 1997. This represented $252,311 in net earnings.

With the dramatic increase in revenue growth, expenses have increased accordingly with the cost of manufacturing products sold being the single largest expense and includes salaries, wages, benefits, materials, occupancy and administrative expenses associated with production of TCT's products. It has fallen from 52.8% to 50.7% as a percentage of product sales. The second greatest expense is administration and sales, which as a percentage of product sales has also decreased from 23% to 21%.

Expenses related to oil & gas production were significantly higher $122,902 on $69,259 in oil & gas sales compared to the previous year which was sales of $202,286 with production costs of $65,054. Weather played an integral part in the added expenses, which include reconstruction of roads and reworking of the wells themselves. Lower oil prices resulted in an oil & gas inventory write down of approximately $35,000.

Provision for future income taxes is a line item insisted upon by our Auditors. It is a non-cash item and no money has been paid to the Federal Government for income taxes.

TCT conducts the majority of its business in the U.S. Accordingly, it tends to pay its U.S. accounts payable out of revenues generated from U.S. sales. This enables TCT to reduce currency and foreign exchange rate risk.

The Charge Air Coolers manufactured by TCT offer many advantages to the end user. Decreased emissions, more horsepower and increased fuel economy are the most evident advantages. These are benefits which all end users seek to take advantage of whenever possible. The management of Thermal Control Technologies Corp. feel that a recession would not significantly affect the Company's operations.

## MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

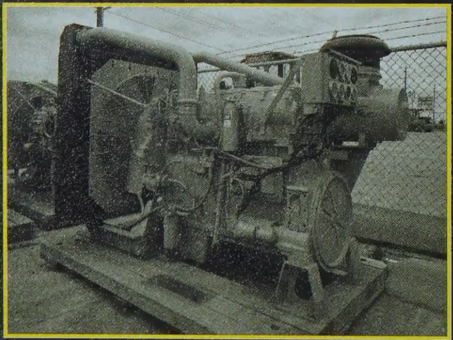
The accompanying consolidated financial statements of Thermal Control Technologies Corp. and all information in the Annual Report is the responsibility of management. The consolidated financial statements have been prepared in accordance with Generally Accepted Accounting Practices. Where necessary, estimates of transactions that were incomplete at the year-end have been made by management. Financial information throughout the Annual Report is consistent with financial statements.

Management maintains appropriate accounting and internal control systems to provide a reasonable assurance that transactions are properly authorized, assets are safe-guarded and to facilitate the preparation of relevant, reliable financial information on a timely basis.

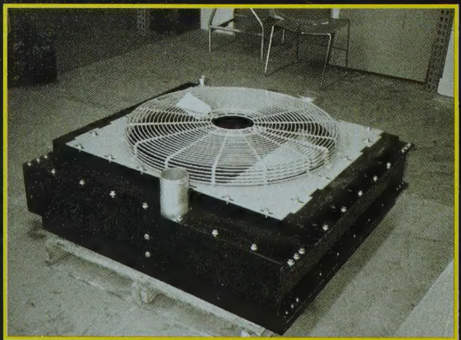
Dick Cook Schulli, the Corporation's external auditors have conducted an examination of the consolidated financial statements in accordance with generally accepted auditing standards. Their report appears in the following section.

The Board of Directors is responsible for ensuring that management fulfills its responsibility for financial reporting and internal control. The Board exercises this responsibility through the Audit Committee of the Board. This committee, comprised of a majority of Directors who are not employees of the Corporation, meets with management and external auditors to satisfy itself that management's responsibilities have been properly discharged. These financial statements have been approved by the Board on the recommendation of the Audit Committee.

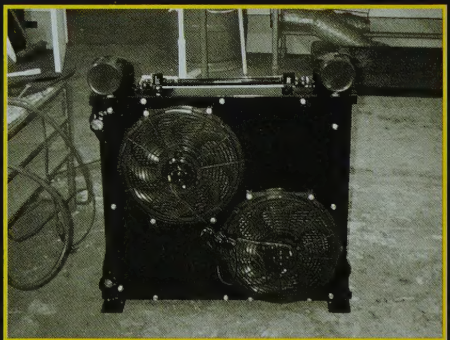




*Caterpillar Gen-Set with complete stacked TCT cooling system. Custom built for Finning (Canada) in Edmonton*



*Stacked unit for the Gen-Set on the left. Components: CAC radiator, shroud, fan, internal surge tank.*



*Custom cooling package specifically designed for bus application, consisting of radiator, CAC, shroud and fans.*

## AUDITORS REPORT

**To the Shareholders of Thermal Control Technologies Corp.:**

We have audited the consolidated balance sheets of Thermal Control Technologies Corp. (formerly Redux Energy Corporation) as at March 31, 1998 and 1997 and the consolidated statements of earnings and retained earnings and changes in financial position for the years then ended. These consolidated financial statements are the responsibility of the corporation's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation.

In our opinion these consolidated financial statements present fairly, in all material respects, the financial position of the corporation as at March 31, 1998 and 1997 and the results of its operations and the changes in its financial position for the years then ended in accordance with Canadian generally accepted accounting principles.

Dick Cook Schulli

CHARTERED ACCOUNTANTS

Calgary, Alberta
June 29, 1998

**THERMAL CONTROL TECHNOLOGIES CORP.**
(formerly Redux Energy Corporation)

**CONSOLIDATED BALANCE SHEET**

As at March 31, 1998 and 1997

| | 1998 | 1997 |
|---|---|---|
| **ASSETS** | | |
| **Current** | | |
| Cash and short term deposits | $ 3,232,819 | $ 25,423 |
| Accounts receivable – Note 2 | 1,004,898 | 400,834 |
| Inventory | 852,176 | 452,118 |
| Prepaid expenses | 276,225 | 73,627 |
| | 5,366,118 | 952,002 |
| **Directors' loans** – Note 3 | 529,750 | - |
| **Property, plant and equipment -** Note 4 | 10,733,745 | 3,175,237 |
| **Goodwill -** Note 5 | 819,897 | 866,936 |
| **Other assets** – Note 6 | 1,306,786 | 175,096 |
| | $ 18,756,296 | $ 5,169,271 |
| **LIABILITIES** | | |
| **Current** | | |
| Bank indebtedness – Note 7 | $ 1,613,722 | $ - |
| Accounts payable and accrued liabilities | 1,303,321 | 693,673 |
| Deferred income - Note 8 | - | 252,311 |
| Note payable – Note 9 | 1,100,500 | - |
| Current portion of long-term debt - Note 10 | 26,092 | 20,945 |
| | 4,043,635 | 966,929 |
| **Provision for future income taxes** | 343,000 | - |
| **Long-term debt -** Note 10 | 49,715 | 31,990 |
| **Debentures payable** – Note 11 | 7,000,000 | - |
| | 11,436,350 | 998,919 |
| **SHAREHOLDERS' EQUITY** | | |
| **Share capital -** Note 12 | 5,686,281 | 3,630,940 |
| **Cumulative translation adjustments** | (15,500) | - |
| **Retained earnings** | 1,649,165 | 539,412 |
| | 7,319,946 | 4,170,352 |
| | $ 18,756,296 | $ 5,169,271 |

**Approved by the Board:**

__________________, **Director**

__________________, **Director**

*See accompanying notes*

**THERMAL CONTROL TECHNOLOGIES CORP.**
(formerly Redux Energy Corporation)

## CONSOLIDATED STATEMENT OF EARNINGS AND RETAINED EARNINGS

For the years ended March 31, 1998 and 1997

| | 1998 | 1997 |
|---|---|---|
| **Revenue** | | |
| Product sales | $ 6,986,024 | $ 1,739,702 |
| Oil and gas, net of royalties | 69,259 | 202,286 |
| Interest | 52,001 | - |
| | 7,107,284 | 1,941,988 |
| **Expenses** | | |
| Cost of manufacturing product sold | 3,543,971 | 918,421 |
| Oil and gas production | 122,902 | 65,054 |
| Administrative and sales | 1,463,380 | 400,541 |
| Amortization and depletion | 293,179 | 201,248 |
| Long-term financing costs | 203,433 | 14,803 |
| Operating line interest | 27,666 | - |
| | 5,654,531 | 1,600,067 |
| **Earnings before income taxes** | 1,452,753 | 341,921 |
| **Provision for future income taxes** – Note 13 | 343,000 | - |
| **Net earnings** | 1,109,753 | 341,921 |
| **Retained earnings,** beginning of year | 539,412 | 197,491 |
| **Retained earnings,** end of year | $ 1,649,165 | $ 539,412 |
| **Earnings per share** | | |
| Basic - pre tax | $ 0.12 | $ 0.03 |
| - after tax | 0.09 | 0.03 |
| Fully diluted | | |
| - pre tax | 0.11 | - |
| - after tax | 0.08 | - |
| **Cash flow per share** | $ 0.15 | $ 0.05 |

*See accompanying notes*

**THERMAL CONTROL TECHNOLOGIES CORP.**
(formerly Redux Energy Corporation)

## CONSOLIDATED STATEMENT OF CHANGES IN FINANCIAL POSITION

For the years ended March 31, 1998 and 1997

| | | 1998 | 1997 |
|---|---|---|---|
| **Source (use) of cash:** | | | |
| **Operating activities** | | | |
| Net earnings | | $ 1,109,753 | $ 341,921 |
| Add items not affecting cash: | | | |
| Cumulative translation adjustment | | (15,500) | - |
| Depletion and amortization | - resource assets | 18,000 | 17,961 |
| | - manufacturing assets | 228,140 | 85,216 |
| | - goodwill | 47,039 | 47,038 |
| | - pre-commencement costs | 51,694 | 51,033 |
| | - new product development | 74,830 | - |
| | - debenture financing costs | 41,090 | - |
| Provision for future income taxes | | 343,000 | - |
| | | 1,898,046 | 543,169 |
| Net change in non-cash working capital | | 251,117 | (35,184) |
| | | 2,149,163 | 507,985 |
| **Financing activities** | | | |
| Proceeds from debentures issued | | 7,000,000 | - |
| Costs of issuing debenture | | (745,360) | - |
| Proceeds on issuance of common shares | | 2,055,341 | 2,536,408 |
| Cost of issuing shares | | - | (379,579) |
| Advances to shareholders | | (529,750) | - |
| Proceeds from long-term debt | | 48,872 | 50,355 |
| Repayment of long-term debt | | (26,000) | (335,931) |
| | | 7,803,103 | 1,871,253 |
| **Investing activities** | | | |
| Acquisition of property, plant and equipment | | (7,804,648) | (2,194,041) |
| Cost of acquiring balance of subsidiary | | - | (175,000) |
| New product development costs | | (553,944) | - |
| | | (8,358,592) | (2,369,041) |
| **Increase in cash** | | 1,593,674 | 10,197 |
| **Cash and equivalents,** beginning of year | | 25,423 | 15,226 |
| **Cash and equivalents,** end of year | | $ 1,619,097 | $ 25,423 |
| **Cash and equivalents composition** | | | |
| Cash and short term deposits | | $ 3,232,819 | $ 25,423 |
| Bank indebtedness | | (1,613,722) | - |
| | | $ 1,619,097 | $ 25,423 |

*See accompanying notes*

**THERMAL CONTROL TECHNOLOGIES CORP.**
(formerly Redux Energy Corporation)

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

For the years ended March 31, 1998 and 1997

## Note 1 - Significant Accounting Policies

### (a) Consolidation

The corporation was the result of the amalgamation on October 1, 1997 of Redux Energy Corporation and its wholly owned Canadian subsidiary, Thermal Control Technologies Corp. (TCT-Canada). Upon amalgamation the amalgamated corporation changed its name to Thermal Control Technologies Corp.

The consolidated financial statements include the results of operations of the corporation and its 100% owned subsidiaries. Thermal Control Technologies Corp. (TCT-Canada) to the date of amalgamation and Thermal Control Technologies Corp. (TCT-US).

TCT-US was acquired in stages. At April 1, 1995 the corporation owned 51% of TCT-US. An additional 34% was acquired during fiscal 1996 and the remaining 15% was acquired in September of 1996.

For accounting purposes 100% of the operation of TCT-US are included. No provision for an allocation to the minority interests is made as it was determined that the corporation was fully responsible for the losses of TCT-US during the period of less than 100% ownership.

### (b) Property, plant and equipment

The corporation follows the full cost method of accounting for oil and gas operations whereby all costs of exploring for and developing petroleum and natural gas reserves are capitalized. Costs include lease acquisition costs, geological and geophysical costs, lease rentals on non-producing properties, and costs of drilling both productive and non-productive wells. Depletion of such costs, net of proceeds from minor disposals of property, and depreciation of production equipment and facilities is calculated on the unit-of-production method based upon estimated proven reserves. Costs of unproven properties are excluded from the depletion calculation until it is determined whether or not proven reserves are attributable to the properties.

The corporation employs a ceiling test annually to determine the limitation on capitalized costs. Such costs are generally limited to the value of the future net revenues from estimated production of proved reserves based upon current prices and costs, and the cost of unproved properties. Future net revenues are calculated after deducting general and administration expenses, financing costs and income taxes. In the current year, prices as of October 1, 1997 have been used in determining future values for the ceiling test.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

For the years ended March 31, 1998 and 1997

**Note 1 - Significant Accounting Policies - Continued**

**(b) Property plant and equipment - Continued**

Estimated future costs of restoring the corporation's oil and gas properties are anticipated to be less than the disposal value of the equipment located on the well. Accordingly, a provision for site restoration has not been provided for as there is no provision for residual value for equipment in calculating depletion.

Cost of manufacturing facilities and equipment include direct acquisition costs, freight and fees. It also includes internal costs for testing, assembly and travel related to the acquisition and installation of the equipment.

Manufacturing rights are amortized on a straight-line basis over twenty-five years effective with the start of production on October 1, 1995. Other manufacturing assets are amortized at rates of 4% to 30%, such rates are designed to amortize the cost of these assets over their estimated useful lives.



**(c) Pre-commencement of business costs**

The corporation capitalized all pre-commencement of business costs associated with the manufacturing business. Effective with the completion of the product and commencement of commercial production, these costs are being amortized on a straight-line basis over five years.

**(d) Goodwill**

Goodwill represents the excess of the consideration paid over the net value of the assets acquired in the acquisition of TCT-US. Amortization is provided for on a straight-line basis over twenty years.

**(e) Inventory**

Product inventory is carried at the lower of cost and net realizable value. Oil and gas inventory is valued at market.

**(f) Foreign currency translation**

Transactions in foreign currencies are translated at rates in effect on the dates of the transactions. Current assets and liabilities have been translated at the rates of exchange prevailing at the balance sheet dates. Gains or losses arising on translation are charged or credited to expense.

**Note 1 - Significant Accounting Policies - Continued**

**(g) Earnings per share**

Basic earnings per share have been calculated on the weighted average number of shares outstanding during the year. Fully diluted earnings per share have not been disclosed because effect is not significant.

**(h) Revenue recognition**

The corporation recognized revenues on contracts to manufacture special orders of product on a percentage of completion basis.

**(i) Share capital**

Share capital has been reduced by certain specific costs relating to issuing shares and direct internal administrative costs that management considered directly related to raising the share capital.

**(j) New product development costs**

The corporation capitalizes certain salaries and expenses related to the development of new products. Capitalized costs are amortized over a period of five years on a straight-line basis.

**(k) Prepaid expenses**

The corporation has incurred certain expenses in connection with the development of promotional material which it has included in prepaid expenses and is amortized over a period of one year commencing January 1, 1998.

**(l) Debenture financing**

Costs incurred in connection with the issuing of debentures are capitalized and amortized on a straight-line basis over the five year term of the debenture.

THERMAL CONTROL TECHNOLOGIES CORP.
(formerly Redux Energy Corporation)

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

For the years ended March 31, 1998 and 1997

**Note 1 - Significant Accounting Policies - Continued**

**(m) Financial instruments**

Financial Instruments

Financial instruments of the corporation include temporary investments, accounts and notes receivable, accounts and notes payable, bank loans, long-term debt and debentures payable.

Financial instruments are originally recorded at cost. Cost is adjusted if circumstances indicate either an other than temporary decline in a financial asset or changes affecting interest rates relating to fixed term debt. Unless otherwise indicated, the fair values of the financial instruments included in the consolidated financial statements approximate their carrying values.

Credit risk

The corporation has a large number of diverse customers which minimizes concentration of credit risk.



**Note 2 - Accounts Receivable**

Accounts receivable consists of the following:

| | 1998 | 1997 |
|---|---|---|
| Trade receivables | | |
| Canada | $ 169,020 | $ 102,375 |
| Less allowance for doubtful accounts | (14,000) | - |
| | 155,020 | 102,375 |
| United States | 684,487 | 163,710 |
| Less allowance for doubtful accounts | (16,279) | - |
| | 668,208 | 163,710 |
| Other | | |
| Canada – goods and services taxes recoverable | 125,350 | 50,568 |
| Other | 56,320 | 84,181 |
| | 181,670 | 134,749 |
| | $ 1,004,898 | $ 400,834 |

## Note 3 - Directors' Loans

During the period ending March 31, 1998, the corporation loaned an aggregate of $529,750 to three directors to enable them to purchase common shares. The loans are unsecured, non-interest bearing and are due July 14, 2002.

## Note 4 - Property, Plant and Equipment

Property, plant and equipment consists of the following:

| | 1998 Cost | 1998 Accumulated Amortization | 1998 Net Book Value | 1997 Net Book Value |
|---|---|---|---|---|
| **Manufacturing assets** | | | | |
| Manufacturing equipment | $ 7,527,450 | $ 269,616 | $ 7,257,834 | $ 2,388,272 |
| Manufacturing rights | 103,689 | 12,960 | 90,729 | 95,913 |
| Other equipment | 543,295 | 201,231 | 342,064 | 194,308 |
| Land | 739,216 | - | 739,216 | - |
| Building | 194,358 | - | 194,358 | - |
| | 9,108,008 | 483,807 | 8,624,201 | 2,678,493 |
| **Resource assets** | 668,138 | 189,394 | 478,744 | 496,744 |
| **Patents** | 1,672,782 | 41,982 | 1,630,800 | - |
| | $ 11,448,928 | $ 715,183 | $ 10,733,745 | $ 3,175,237 |

In calculating the annual charge for depletion of resource assets, costs of non-producing properties aggregating $329,000 have been excluded from the depletion base.

The patents have been acquired from a related party (see Note 9).

Included in the costs capitalized for manufacturing assets is $132,102 (1997 - $51,500) of salaries and expenses relating to the acquisition, testing and construction of equipment and facilities.

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

For the years ended March 31, 1998 and 1997

**Note 5 - Goodwill**

| | 1998 | 1997 |
|---|---|---|
| Balance, beginning of year | $ 940,787 | $ 765,787 |
| Cost of acquisition of TCT-US | - | 175,000 |
| | 940,787 | 940,787 |
| Accumulated amortization | 120,890 | 73,851 |
| | $ 819,897 | $ 866,936 |

The acquisition of the remaining 15% of TCT-US in fiscal 1997 has been allocated entirely to goodwill as the corporation had no identifiable net assets at that time.

**Note 6 - Other Assets**

| | 1998 | 1997 |
|---|---|---|
| Pre-commencement of business costs | $ 252,809 | $ 252,809 |
| Accumulated amortization | (129,407) | (77,713) |
| | 123,402 | 175,096 |
| New product research and development costs | 553,944 | - |
| Accumulated amortization | (74,830) | - |
| | 479,114 | - |
| Debenture issue costs | 745,360 | - |
| Accumulated amortization | (41,090) | - |
| | 704,270 | - |
| | $ 1,306,786 | $ 175,096 |

During the year the corporation capitalized certain salaries and expenses directly related to the development of new products in the amount of $245,744 (1997 - $ Nil). It also capitalized $45,000 of salaries and expenses related to the issuing of debentures.

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

For the years ended March 31, 1998 and 1997

### Note 7 - Bank Indebtedness

The bank indebtedness is secured by an assignment of accounts receivable and inventory and bears interest at varying rates. Details are as follows:

| | 1998 | 1997 |
|---|---|---|
| Demand loan bearing interest at prime plus 0.5% per annum | $ 105,000 | $ - |
| U.S.$ denominated bank loan bearing interest at U.S. base rate plus 0.5% per annum. ($270,000 U.S.) | 383,400 | - |
| U.S.$ denominated bank loan bearing interest at the bank's reference rate plus 1.25% per annum. ($472,175 U.S.) | 670,488 | - |
| | 1,158,888 | - |
| Excess of cheques written over funds on deposit | 454,834 | - |
| | $ 1,613,722 | $ - |

### Note 8 - Deferred Income

During the current year the corporation acquired $3,837,000 ($2,703,000 U.S.) (1997 - $1,890,000 ($1,350,000 U.S.)) of equipment from one customer in exchange for the sale of products of the same amount.

As at March 31, 1997, the corporation had received all the manufacturing equipment but did not complete delivery of all the product resulting in deferred income of $252,311.

## Note 9 - Note Payable

Effective October 1, 1997 the corporation acquired the rights to the patents for the charge air cooler systems from an officer of TCT-US. The patents are pending in Canada, the United States and other countries.

The total purchase price for the patents was $1,645,000 ($1,175,000 US) and it was satisfied by paying $284,000 ($200,000 US) cash, issuing 195,862 common shares for an aggregate value of $284,000 and issuing a promissory note for $1,100,500 ($775,000 US) payable on January 15, 1999.

The vendor has the right to accept all cash or a combination of cash and shares for the amount due.

## Note 10 - Long-Term Debt

| | 1998 | 1997 |
|---|---|---|
| **TCT**<br>Finance contracts repayable in aggregate monthly instalments of $1,399 including interest at 8.9% per annum and secured by specified automobiles. | $ 24,778 | $ 38,666 |
| **TCT-US**<br>Finance contracts repayable in aggregate monthly instalments of $1,291 including interest at varying rates, secured by automobiles and maturing on varying dates. | 51,029 | 14,269 |
| | 75,807 | 52,935 |
| Portion due within one year | 26,092 | 20,945 |
| | $ 49,715 | $ 31,990 |

The balance of the long-term debt will be repaid in 2000 - $33,000 and 2001 - $17,000.

**Note 11 - Debentures Payable**

Pursuant to a trust indenture dated December 19, 1997, and an agency agreement dated December 10, 1997, the corporation completed a public offering issuing $7,000,000 in principal amount of 8% convertible unsecured subordinated debentures. The debentures are dated December 19, 1997, mature on December 19, 2002 and bear interest at a rate of 8% per $1,000 principal amount of debentures payable on June 30 and December 31 of each year beginning June 30, 1998. The debentures may not be redeemed by the corporation prior to December 19, 1999. The debentures are direct obligations of the corporation and are unsecured and subordinated to secured indebtedness of the corporation. The debentures are convertible at the option of the holder into common shares of the corporation at any time after January 31, 1998 and before the close of business on the last business day prior to the earlier of the date fixed for redemption or the maturity date at the conversion price of $1.60 per common share, being a rate of 625 common shares per $1,000 principal amount of debentures, subject to adjustment in certain events.

**Note 12 - Share Capital**

Authorized:
Unlimited number of:
Voting common shares
Non-voting preferred shares

| | Shares | Amount |
|---|---|---|
| Voting common shares issued: | | |
| Balance, March 31, 1996 | 9,428,524 | $ 1,474,111 |
| Directors' options | 231,760 | 59,401 |
| Private placement | 200,000 | 332,000 |
| Rights offering | 1,604,754 | 2,005,942 |
| Warrants exercised | 103,011 | 139,065 |
| Share issuance costs | - | (379,579) |
| Balance, March 31, 1997 | 11,568,049 | 3,630,940 |
| Acquisition of patents | 195,862 | 280,000 |
| Directors' options | 1,230,000 | 600,750 |
| Warrants exercised | 694,567 | 937,665 |
| Private placement | 183,750 | 294,000 |
| Share issuance costs | - | (57,074) |
| Balance, March 31, 1998 | 13,872,228 | $ 5,686,281 |

As at March 31, 1997, the corporation has the following warrants outstanding:

### Note 12 - Share Capital - Continued

| Quantity | Price | Expiry Date |
|---|---|---|
| 100,000 | $ 2.20 | April 19, 1998 |

In addition, the corporation has the following options outstanding at March 31, 1997:

| Quantity | Date Granted | Expiry Date | Price |
|---|---|---|---|
| 97,335 | August 6, 1996 | August 6, 2001 | $1.30 |
| 768,000 | September 12, 1997 | August 28, 2002 | $1.32 |
| 75,000 | September 17, 1997 | August 28, 2002 | $1.32 |
| 120,000 | September 29, 1997 | September 5, 2002 | $1.60 |
| 25,000 | November 21, 1997 | November 21, 2002 | $1.32 |

### Note 13 - Provision for Future Income Taxes

The corporation's provision for future income taxes varies from amounts determined by applying Canadian Federal and Provincial statutory rates to income as follows:

| | 1998 % | 1997 % |
|---|---|---|
| Combined statutory rates | 44.6 | 44.6 |
| Utilization of loss carryforwards | (10.2) | (33.8) |
| Non deductible expenses | .2 | .2 |
| U.S./Canada rate difference | (11.0) | (11.0) |
| **Provision for future taxes** | 23.6 | 0.0 |

The corporation is not currently taxable as it has sufficient tax depreciation and other deductions to reduce current taxable income to nil.

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## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the years ended March 31, 1998 and 1997

### Note 14 - Segmented Information

The corporation operates in two distinct business segments. The first is the sale of oil and gas reserves. The second is the manufacture and sale of charge-air coolers. The resource segment is carried on in Western Canada while the manufacturing operation is carried on principally in the United States. Information concerning these segments is as follows:

| **Operations:** | **1998** | **1997** |
|---|---|---|
| **Resource** | | |
| Oil and gas sales, net of royalties | $ 69,259 | $ 202,286 |
| **Expenses** | | |
| Production costs | 122,902 | 65,054 |
| General and administration | - | 90,680 |
| Depletion and amortization | 18,000 | 17,961 |
| | 140,902 | 173,695 |
| **Net earnings (loss)** | $ (71,643) | $ 28,591 |
| **Manufacturing:** | | |
| Sales | $ 6,986,024 | $ 1,739,702 |
| Cost of sales | 3,376,357 | 918,421 |
| | 3,609,667 | 821,281 |
| **Expenses** | | |
| Amortization: | | |
| Property, plant and equipment | 228,140 | 85,215 |
| Deferred costs | 167,614 | 51,033 |
| Goodwill | 47,039 | 47,039 |
| General and administration | 1,463,380 | 309,861 |
| Interest on long-term debt | 231,099 | 14,803 |
| | 2,137,272 | 507,951 |
| **Net earnings** | $ 1,472,395 | $ 313,330 |

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**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

For the years ended March 31, 1998 and 1997

**Note 14 - Segmented Information - Continued**

| | March 31, 1997 | |
|---|---|---|
| | Resource | Manufacturing |
| **Identifiable assets:** | | |
| Directors' loans | $ - | $ 529,750 |
| Current assets | $ 12,565 | $ 5,353,553 |
| Other assets | $ - | $ 1,306,786 |
| Property, plant and equipment | $ 478,744 | $ 10,617,745 |
| Goodwill | $ - | $ 819,897 |
| Current liabilities | $ 2,466 | $ 3,925,169 |
| Long-term debt | $ - | $ 49,149 |
| Debenture payable | $ - | $ 7,000,000 |

**Note 15 - Differences Between Canadian GAAP and United States GAAP**

The consolidated financial statements for the corporation have been prepared in accordance with accounting principles generally accepted in Canada ("Canadian GAAP"). Set out below is a summary of the differences between Canadian and United States generally accepted accounting principles ("US GAAP"). The differences primarily relate to certain expenses capitalized and amortized under Canadian GAAP but expensed as incurred under U.S. GAAP



**Earnings Reconciliation**

| | Year ended March 31, | |
|---|---|---|
| | 1998 | 1997 |
| Net earnings under Canadian GAAP | $ 1,109,753 | $ 341,921 |
| U.S. differences - | | |
| Pre commencement expense amortization | 51,694 | 51,033 |
| Product development costs | (479,114) | (68,600) |
| Salaries included in financing costs | (45,000) | - |
| Prepaid promotional items | (248,328) | - |
| Tax effect of share issue costs | - | (169,368) |
| Tax benefit of losses on acquisition of TCT-US which reduces goodwill on acquisition under US GAAP | (165,000) | (131,000) |
| Net earnings under US GAAP | $ 224,005 | $ 23,986 |
| Earnings per share | | |
| Primary | $ 0.02 | $ 0.00 |
| Fully diluted | $ 0.02 | $ 0.00 |

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